

**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

In the Matters of	)	
	)	
Federal-State Joint Board on	)	
Universal Service;	)	
Promoting Deployment and	)	CC Docket No. 96-45
Subscribership in Unserved	)	
and Underserved Areas, Including	)	
Tribal and Insular Areas	)	

**PUERTO RICO TELEPHONE COMPANY WHITE PAPER:  
PROPOSED INTERIM INSULAR MECHANISM**

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The Telecommunications Act of 1996 (“Telecommunications Act” or “Act”) requires the Federal Communications Commission (“FCC” or “Commission”) to ensure that every American has access to affordable telecommunications services that are reasonably comparable with those available in urban areas.<sup>1</sup> To achieve this national objective, Congress explicitly directed the Commission to focus its universal service support mechanisms on rural, insular, and high-cost areas.<sup>2</sup> While the Commission has acknowledged “Congressional intent ... support[ing] the adoption of special mechanisms by which to calculate support for insular areas;”<sup>3</sup> it has nonetheless failed to satisfy Congress’ mandate with respect to insular areas despite the passage of almost nine years and the establishment of specific mechanisms for high-cost areas<sup>4</sup> and rural areas.<sup>5</sup>

Immediate Commission action to address the universal service needs of insular areas, particularly non-rural insular areas, is both statutorily required and squarely in the public interest.

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<sup>1</sup> 47 U.S.C. § 254(b)(3) (2005); *see also Federal State Joint Board on Universal Service*, Ninth Report and Order, 14 FCC Rcd 20432, 20439, ¶ 12 (1999) (“*Ninth Report and Order*”).

<sup>2</sup> 47 U.S.C. § 254(b)(3).

<sup>3</sup> *Rural Health Care Support Mechanism*, Second Report and Order, Order on Reconsideration, and Further Notice of Proposed Rulemaking, WC Docket No. 02-60, FCC 04-289, ¶ 42 (Dec. 17, 2004).

<sup>4</sup> *See Ninth Report and Order*.

<sup>5</sup> *Federal-State Joint Board on Universal Service*, Fourteenth Report and Order, Twenty-Second Order on Reconsideration, and Further Notice of Proposed Rulemaking, 16 FCC Rcd 11244 (2001) (“*Rural Task Force Order*”). The FCC has defined “rural carrier” and “rural incumbent local exchange carrier” as incumbent local exchange carriers that meet the definition of a rural telephone company set forth in section 153(37) of the Act. 47 U.S.C. § 153(37) (2005). The FCC has asked the Joint Board to consider a successor plan to the *Rural Task Force Order*, and the Joint Board has solicited comment to that end. *Federal-State Joint Board on Universal Service*, Order, 19 FCC Rcd 11538 (2004) (“*Referral Order*”); *Federal-State Joint Board on Universal Service Seeks Comment on Certain of the Commission’s Rules Relating To High-Cost Universal Service Support*, CC Docket No. Public Notice, 96-45, FCC 04J-2 (Aug. 16, 2004).

Insular areas have geographic, climatic, economic, and demographic conditions that make the construction of infrastructure and delivery of service challenging and costly. While the majority of insular areas are rural and thus able to receive needed support through the FCC's rural universal service mechanism, non-rural insular areas, like Puerto Rico, are completely overlooked and desperately in need of support. Recent revisions to the high-cost mechanism have compounded matters further by eliminating previous high-cost loop support for non-rural insular carriers.

Currently, the telephone penetration rate in Puerto Rico stands below 70 percent – far below the national average of 94 percent. Some isolated communities on the island have no telephone service at all. Like rural areas, the delivery of telephone service in Puerto Rico is subject to significant costs – from shipping and storing needed equipment and supplies, conquering and reconquering rough terrain and heavy vegetation, and repairing and replacing equipment damaged by corrosive salt air and tropical weather. Added to this are the economic realities in Puerto Rico:

- Per capita income in Puerto Rico is two-thirds that of the poorest state;
- Over half of Puerto Rico's residents live below the poverty line; and
- Puerto Rico's cost of living far exceeds the national average.

Puerto Rico would thus seem to be precisely the type of area that should be receiving high cost universal support. Yet, it currently receives zero. This is true despite the fact that Puerto Rico received approximately \$50 million in annual universal service loop funding prior to the adoption of a non-rural mechanism that lumped Puerto Rico into a mainland-based approach.

The Puerto Rico Telephone Company (“PRT”) accordingly renews its plea that the Commission move promptly to adopt a non-rural insular mechanism to address deserving but overlooked areas such as Puerto Rico. Toward this end, this White Paper provides a comprehensive overview of the compelling legal and public interest reasons supporting such a mechanism, as well as a history of the multiplicity of FCC proceedings that initiated, but never completed, addressing Congress’ mandate for insular support. This issue is currently ripe and ready for action in several dockets.

This White Paper also offers a proposed universal service mechanism for non-rural insular areas that is patterned after the existing mechanism for rural areas, an established mechanism that provides known results. Significantly, this interim mechanism would have a minimal impact on the total size of the universal service fund, and would only restore funding previously received by insular carriers. Under this proposal, non-rural insular carriers would be eligible to receive high-cost loop support for those study areas in which average loop costs, based on actual costs, exceed a set percentage threshold of the national average loop cost. This mechanism would remain in place until the Commission adopted a forward-looking cost mechanism that accurately identifies and projects the cost to deliver service to all non-rural insular areas.

The people of Puerto Rico deserve the affordable telecommunications services that other Americans have long enjoyed. By finally adopting a non-rural insular mechanism, the FCC can make that happen.

## **I. BACKGROUND**

This section provides a comprehensive review of Congressional and Commission action since 1996 with respect to the affordability of, and accessibility to, telecommunications services in insular areas. The FCC's procedural and substantive actions demonstrate a continued recognition of the plight of insular areas, without any corresponding tangible actions to target or direct universal service support to these needy communities. In fact, the FCC's shifts in universal service policy have only compounded the challenges faced by insular areas, particularly non-rural insular providers.

### **A. Section 254 of the Telecommunications Act of 1996**

Section 254 of the Telecommunications Act of 1996 “codifie[s] the historical commitment of the Commission ... to promote universal service.”<sup>6</sup> It requires the FCC, after obtaining a recommendation from the Federal-State Joint Board on Universal Service (“Joint Board”), to create “specific, predictable, and sufficient [support] mechanisms to preserve and advance universal service.”<sup>7</sup> The fundamental goal of this universal service provision is to ensure that consumers in “rural, insular, and high-cost areas” have access to telecommunications services at rates that are “reasonably comparable to rates charged for similar services in urban areas.”<sup>8</sup> Universal service support must be “explicit and sufficient to achieve the purposes of this section.”<sup>9</sup> The specific inclusion of insular communities in section 254 represents a pointed

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<sup>6</sup>*Federal-State Joint Board on Universal Service*, Order on Remand, Further Notice of Proposed Rulemaking, and Memorandum Opinion and Order, 18 FCC Rcd 22559, 22563, ¶ 5 (“*Remand Order*”).

<sup>7</sup> 47 U.S.C. § 254(b)(5).

<sup>8</sup> *Id.* § 254(b)(3).

<sup>9</sup> *Id.* § 254(e).

congressional mandate that universal support mechanisms be in place to benefit citizens living in U.S. territories around the globe.<sup>10</sup>

## **B. Joint Board Insular Panel and First Recommended Decision**

Consistent with the Act, the Commission's initial referral to the Joint Board in 1996 requested that the Joint Board make a recommendation addressing universal service issues, including those that affect the provision of telecommunications service in insular areas.<sup>11</sup> In its First Recommended Decision, the Joint Board highlighted that the obligation of "the Joint Board and the Commission [was] to consider consumers of insular areas ... when developing support mechanisms for consumer access to telecommunications and information services."<sup>12</sup> The Joint Board further "recognize[d] the special circumstances faced by carriers and consumers in the insular areas of the United States," pointing specifically to the increased costs of shipping and annual damage from tropical storms as examples of the difficulties faced in insular areas.<sup>13</sup> Non-rural insular areas were referred to as examples of insular areas facing these unique challenges. Nevertheless, based on the record available at that time, the Joint Board recommended only that

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<sup>10</sup> See 142 CONG. REC. H1175 (daily ed. Feb. 1, 1996) (statement of Rep. Underwood); *see also* H.R. REP. NO. 104-458, at 131 (1996) (noting the addition of insular areas to the "list of consumers to whom access to telecommunications and information services should be provided.")

<sup>11</sup> See *Federal-State Joint Board on Universal Service*, Notice of Proposed Rulemaking and Order Establishing Joint Board, 11 FCC Rcd 18092, 18112, ¶ 38 (1996).

<sup>12</sup> *Federal-State Joint Board on Universal Service*, Recommended Decision, 12 FCC Rcd 87, 306, ¶ 430 (1996) ("1996 Recommended Decision").

<sup>13</sup> *Id.* at 306, ¶ 434.

*rural* insular carriers should not be shifted to a forward-looking cost-based model until there was “further review of their situation.”<sup>14</sup>

### **C. Universal Service First Report and Order**

In the May 1997 Report and Order on universal service, the FCC recognized the formidable challenges facing insular areas.<sup>15</sup> The FCC indicated its intent that all carriers should ultimately transition to a forward-looking cost model once a model could be developed that met the goals of the Telecommunications Act.<sup>16</sup> However, it held that all rural carriers would continue to receive universal service support based on an historical cost mechanism until further review.<sup>17</sup> At this time, the FCC did not specifically create a separate mechanism that would apply to non-rural insular areas based on its belief that non-rural insular carriers should possess economies of scale and scope as much as other non-rural carriers.<sup>18</sup> Nevertheless, the FCC pledged to “examine ways to improve subscribership in ... areas” where penetration rates were “particularly low,” explicitly citing Puerto Rico as an example.<sup>19</sup> The Commission did, however,

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<sup>14</sup> *Id.* at 230, ¶ 272.

<sup>15</sup> *Federal-State Joint Board on Universal Service*, Report and Order, 12 FCC Rcd 8776, 8945, 8997, ¶¶ 314, 414 (1997) (“*First Report and Order*”).

<sup>16</sup> *Id.* at 8888, ¶ 199.

<sup>17</sup> *Id.* at 8889, ¶ 203.

<sup>18</sup> *Id.* at 8946, ¶ 315.

<sup>19</sup> *Id.* at 8997, ¶ 415. PRT filed a petition for reconsideration that non-rural insular carriers should be classified as rural under the FCC’s rules. *Federal-State Joint Board on Universal Service, Forward Looking Cost Mechanism for High Cost Support for Non-Rural LECs*, Petition for Reconsideration of Puerto Rico Telephone, CC Docket No. 96-45 (July 17, 1997) (“*PRT Petition for Reconsideration*”). The Commission rejected this petition in a 2004 ruling relying on the findings of the *First Report and Order*. *Federal-State Joint Board on Universal Service*, Order on Reconsideration, CC Docket No. 96-45, FCC 04-237, ¶ 20 (Nov. 29, 2004) (“*Order on Reconsideration*”).



acknowledge the unique character of insular areas, stating that “insular areas generally have subscribership levels that are lower than the national average, largely as a result of income disparity, compounded by the unique challenges these areas face by virtue of their locations.”<sup>20</sup>

#### **D. Unserved and Underserved Proceeding**

The FCC began this examination of areas with low penetration rates in 1999, by opening a proceeding to address the distinctive problems facing both insular areas and tribal lands. In that proceeding, the FCC noted that “telephone penetration rates among low-income consumers, and in insular, high-cost, and tribal lands lag behind the penetration rates in the rest of the country.”<sup>21</sup> The FCC further recognized that “subscribership levels are below the national average in ... certain insular areas.”<sup>22</sup> In 2000, the Commission acted on the tribal lands portion of this proceeding.<sup>23</sup> In doing so, the FCC again pledged to “continue to examine and address the causes of low subscribership in other areas and among other populations, especially among low-income individuals in ... insular areas.”<sup>24</sup> The Commission also noted the need for action in “areas where the cost to deploy telecommunications facilities is significantly above the national

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<sup>20</sup> *First Report and Order*, ¶ 112.

<sup>21</sup> *Federal-State Joint Board on Universal Service: Promoting Deployment and Subscribership in Unserved and Underserved Areas, Including Tribal and Insular Areas*, Further Notice of Proposed Rulemaking, 14 FCC Rcd 21177, 21180, ¶ 5 (1999) (“*Unserved and Underserved Areas Further Notice*”).

<sup>22</sup> *Federal-State Joint Board on Universal Service: Promoting Deployment and Subscribership in Unserved and Underserved Areas, Including Tribal and Insular Areas*, Twelfth Report and Order, Memorandum Opinion and Order, and Further Notice of Proposed Rulemaking, 15 FCC Rcd 12208, 12226, ¶ 32 (2000) (“*Twelfth Report and Order*”).

<sup>23</sup> *Id.* at 12226-27, ¶¶ 32-33.

<sup>24</sup> *Id.* at 12215, ¶ 11.

average.”<sup>25</sup> To date, the Commission has not yet moved forward on these other aspects of the proceeding.

#### **E. Universal Service Ninth Report and Order**

Also in 1999, the Commission adopted its *Ninth Report and Order* in the universal service proceeding, in which it created a forward-looking cost methodology for all non-rural high-cost loop support. Although rural insular carriers maintained their support based upon embedded cost (through the rural support mechanism),<sup>26</sup> non-rural insular carriers, having no insular mechanism of their own, fell under the new methodology by default. This had disastrous results for non-rural insular areas – this decision and its implementation had the effect of eliminating all high-cost loop support for non-rural insular carriers.

The new methodology took a one-size-fits-all approach with respect to calculating the costs of providing service that did not separately address the unique concerns of insular areas. Further, the model was based primarily on mainland inputs and assumptions; no data from insular areas were included in its design.<sup>27</sup> The result was a significant loss of critical support for non-rural insular carriers.<sup>28</sup>

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<sup>25</sup> *Id.*

<sup>26</sup> This finding specifically reserved a decision on rural carriers until “the Commission, the Joint Board, and a Rural Task Force appointed by the Joint Board [had] selected an appropriate methodology for rural support.” *Ninth Report and Order*, 14 FCC Rcd at 20439, ¶ 11.

<sup>27</sup> See *Common Carrier Bureau Seeks Further Comment on Specific Questions in Universal Service Notice of Proposed Rulemaking*, Public Notice, CC Docket No. 96-45, DA 96-1078, Question 41 (July 3, 1996) (asking “[h]ow should support be calculated for those areas (e.g., insular areas and Alaska) that are not included under the proxy model?”); see generally *Federal-State Joint Board on Universal Service, Forward-Looking Mechanism for High Cost Support for Non-Rural LECs*, Tenth Report and Order, 14 FCC Rcd 20156 (1999) (“*Tenth Report and*

Nevertheless, the Commission determined that the synthesis model achieves reasonable results in general, and this finding has been upheld by the courts.<sup>29</sup> The Commission adopted a hold harmless mechanism that continued pre-existing high-cost loop support levels,<sup>30</sup> but phased them out at the rate of one dollar per line per year.<sup>31</sup>

## **F. Rural Task Force**

Subsequent to the *Ninth Report and Order*, the Commission established the Rural Task Force, whose mission was to “identif[y] the issues unique to rural carriers and analyz[e] the appropriateness of proxy cost models for rural carriers.”<sup>32</sup> The Rural Task Force dedicated significant resources to the empirical study of rural carriers, their service areas, and the ability of model-based support to provide sufficient funding.

The Rural Task Force recognized the many operational barriers to providing service in insular areas, including severe weather and the added cost of having to ship all materials.<sup>33</sup> The Rural Task Force recommended, and the FCC implemented, a modified embedded cost support

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*Order*”); Petition for Clarification and/or Reconsideration of the Puerto Rico Telephone Company, Inc., CC Docket No. 96-45, 15 (Jan. 14, 2004). (“*PRT Petition for Clarification*”).

<sup>28</sup> For example, prior to the transition established in the *Ninth Report and Order*, PRT received the second highest amount of high-cost loop support of any jurisdiction nationwide, approximately \$50 million annually. Yet, under the new high-cost support mechanism, all high-cost loop support for Puerto Rico has been eliminated.

<sup>29</sup> *Qwest v. FCC*, 258 F.3d 1191 (10th Cir. 2001); *see also Remand Order*.

<sup>30</sup> *Ninth Report and Order*, 14 FCC Rcd at 20473-79, ¶¶ 77-88.

<sup>31</sup> *Federal-State Joint Board on Universal Service*, Thirteenth Report and Order and FNPRM, 15 FCC Rcd 24422 (1999). (“*Thirteenth Report and Order*”).

<sup>32</sup> *First Report and Order*, 12 FCC Rcd at 8917-18, ¶ 253.

<sup>33</sup> Rural Task Force, White Paper 1, *Rural Task Force Mission and Purpose*, 26-29 (Sept. 1999).

mechanism for all rural carriers.<sup>34</sup> While these modifications addressed the vast majority of insular areas – which are additionally classified as rural – they did not apply to non-rural insular areas.

#### **G. Ninth Report Remand Order**

The FCC reaffirmed its use of model-based support for non-rural carriers in the *Ninth Report Remand Order*. Within that decision, the FCC also denied a petition for reconsideration of the *Ninth Report and Order*, in which PRT sought to be classified as a rural carrier for purposes of universal service funding.<sup>35</sup> In doing so, the FCC explicitly reserved judgment and further deferred the more significant decision as to the universal service needs of insular areas, by delaying consideration of PRT’s broader request that “the Commission create a separate category of ‘non-rural insular’ carriers for purposes of intrastate high-cost support.”<sup>36</sup>

#### **H. November 2004 Universal Service Order on Reconsideration**

In November 2004, the FCC released an order in the universal service docket that, *inter alia*, rejected PRT’s petition for reconsideration of the 1997 *First Report and Order* that had requested that PRT be treated as a rural carrier for purposes of the universal service program.<sup>37</sup> The FCC once more reserved consideration of PRT’s broader request for the adoption of a distinct insular mechanism to a later proceeding. In separate statements, three Commissioners

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<sup>34</sup> *Rural Task Force Order*, 16 FCC Rcd at 11244.

<sup>35</sup> *Remand Order*, 18 FCC Rcd at 22637, ¶ 139. PRT filed a Petition for Reconsideration and/or Clarification of that Order, asking that the Commission clarify the reasoning that was contained in that Order, but not seeking to reverse the Commission’s refusal to classify PRT as a rural carrier. *See PRT Petition for Clarification*.

<sup>36</sup> *Id.*, at n.5 (citation omitted).

<sup>37</sup> *Order on Reconsideration*, CC Docket No. 96-45, FCC 04-237, ¶ 20 (rel. November 9, 2004).

indicated support for the creation of a distinct insular mechanism. Now Chairman Kevin Martin indicated that he believed that the Commission should have granted PRT's proposal to be treated as a rural carrier.<sup>38</sup> Commissioner Michael Copps stated that the Commission was "long past due to address [the insular] aspect of the [Telecommunications Act] and incorporate this concept in [the] universal service support system."<sup>39</sup> Commissioner Jonathan Adelstein also noted that he hoped that the Commission would move forward "expeditiously" in its consideration of the "sufficiency of support for carriers in insular areas."<sup>40</sup> Clearly, there is support among the Commission for action to alleviate the problems faced by insular carriers.

## **II. THE COMMISSION SHOULD ADOPT A NON-RURAL INSULAR MECHANISM IN AN EXPEDITED MANNER**

Based on the record in this proceeding, the Commission should move promptly to establish a non-rural insular universal service mechanism. Congress and the FCC have both previously recognized the unique challenges insular areas face in providing affordable telecommunications services. Yet, the FCC's universal service actions to date have repeatedly overlooked non-rural insular issues. Recent revisions to the high-cost funding methodology have made the need for universal service assistance in these areas even more acute.

This section addresses the compelling legal and public policy reasons supporting prompt Commission action to adopt a non-rural insular universal service mechanism. Part A discusses the Congressional mandate requiring the Commission to address the challenges facing carriers in insular areas. Part B enumerates the public interest factors that support expeditious Commission

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<sup>38</sup> *Id.*, Dissenting Statement of Commissioner Kevin J. Martin.

<sup>39</sup> *Id.*, Concurring Statement of Commissioner Michael J. Copps.

<sup>40</sup> *Id.*, Concurring Statement of Commissioner Jonathan S. Adelstein.

action, including the geographic, economic, and demographic realities that necessitate special treatment for insular areas that are not reflected in the current universal service mechanisms.

**A. The Act Obligates the FCC to Address Non-Rural Insular Areas**

The Telecommunications Act of 1996 recognized the unique challenges faced by carriers serving insular areas and mandated Commission action to address these obstacles. In particular, section 254 clearly requires the Commission to take action to address the unique challenges of providing telecommunications services to insular areas.<sup>41</sup> This provision directs the agency to adopt universal service policies upon the principle that “[c]onsumers in all regions of the Nation, including low-income consumers and those in rural, *insular*, and high-cost areas, should have access to telecommunications and information services.”<sup>42</sup> The reference to insular was not made in passing but rather was specifically added to recognize the unique concerns of these

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<sup>41</sup> While the Act itself does not define “insular,” the FCC proposed in the *Unserved and Underserved Areas Further Notice* to define “insular” as the “islands that are territories or commonwealths of the United States.” *Unserved and Underserved Areas Further Notice*, 14 FCC Rcd at 21233, ¶ 137. Commenters in this proceeding generally agreed. Moreover, this definition is consistent with the definition used by the United States Department of Interior and encompasses all of the areas that have historically been considered insular areas, including Guam, Puerto Rico, the Commonwealth of the Northern Mariana Islands, and the U.S. Virgin Islands. Comments of the National Telephone Cooperative Association, CC Docket 96-45, at 31 (Dec. 17, 1999) (“supports the Commission’s proposed definition of insular areas to include territories or commonwealths of the United States”); Comments of Puerto Rico Telephone Company, CC Docket No. 96-45, at 15 (Dec. 17, 1999); Comments of the Commonwealth of the Northern Mariana Islands, CC Docket No. 96-45, at 12 (Dec. 17, 1999) (“*CNMI Comments*”); see also Definitions of Insular Area Political Organizations, available at [http://www.doi.gov/oia/Islandpages/political\\_types.htm](http://www.doi.gov/oia/Islandpages/political_types.htm) (last viewed Nov. 13, 2004).

<sup>42</sup> 47 U.S.C. § 254(b)(3) (emphasis added).

areas.<sup>43</sup> The provision goes on to instruct the Commission that its universal service policies must ensure that “services should be available at just, reasonable, and affordable rates.”<sup>44</sup>

Other provisions of the Act also compel adoption of an insular mechanism. Section 151 directs the FCC “to make available, so far as possible, to all the people of the United States, without discrimination on the basis of race, color, religion, national origin, or sex, a rapid, efficient Nation-wide . . . wire and radio communication service with adequate facilities at reasonable charges.”<sup>45</sup> The continued unavailability or unaffordability of telecommunications service in insular communities is directly at odds with this clear statutory goal. Similarly, section 706 requires the Commission to “encourage the deployment . . . of advanced telecommunications capability to all Americans.”<sup>46</sup> Obviously, to the extent affordable basic telecommunications services are unavailable in an insular area, the deployment of advanced services are likely to remain an impossibility.

Adhering to these Congressional mandates compels the Commission to establish a non-rural insular mechanism. First, the low penetration rates in non-rural insular areas make clear that affordable access to telecommunications services – the goal mandated by Congress – has not been achieved. Indeed, the factual record reveals that these areas have penetration rates well

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<sup>43</sup> 142 CONG. REC., H1175 (daily ed. Feb. 1, 1996)(statement of Rep. Underwood) (noting that “[when the universal service provision was first drafted, it neglected to mention whether or not it applied to insular areas.”).

<sup>44</sup> 47 U.S.C. § 254(b)(1).

<sup>45</sup> 47 U.S.C. § 151 (2005).

<sup>46</sup> 47 U.S.C. § 706 (2005).

below the national average.<sup>47</sup> While the penetration rate in the mainland United States is 94 percent,<sup>48</sup> the penetration rate in Puerto Rico is below 70 percent,<sup>49</sup> with many areas on that island having levels below 60 percent.<sup>50</sup> In Puerto Rico, some isolated communities have no telecommunications infrastructure at all. These low penetration rates are a particular concern to the Commission because increasing low subscribership levels is one of the fundamental goals of the universal service program.<sup>51</sup> Indeed, the Commission has recognized its obligation to “address instances of low or declining subscribership levels” and take such action as it deems “necessary to fulfill the requirements of section 254.”<sup>52</sup> For example as described above, the Commission initiated a targeted proceeding in the *Unserved and Underserved Areas Further Notice* to explore, among other things, how to improve penetration rates in insular areas.<sup>53</sup>

While low penetration rates are a problem in and of themselves, they also demonstrate another fundamental problem: indirect proof that rates are not affordable. The Commission has concluded that subscribership levels correlate directly to the affordability of rates, finding that

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<sup>47</sup> Comments of the Public Service Commission of the United States Virgin Islands, CC Docket No. 96-45, at 6 (Dec. 17, 1999) (“VIPSC Comments”).

<sup>48</sup> *Telephone Subscribership in the United States*, Federal Communications Commission, Wireline Competition Bureau, 6 (Table 1) (Oct. 26, 2004).

<sup>49</sup> In the last 30 years, the penetration rate in Puerto Rico increased significantly from 25 percent to where it stands today, slightly below 70 percent. Comments of Puerto Rico Telephone Company, CC Docket No. Nos. 96-45, 96-262, at (July 23, 1999).

<sup>50</sup> *PRT Underserved Comments*. Other insular areas also have significantly lower penetration rates than the mainland; the Commonwealth of the Northern Mariana Islands reported a penetration rate of 61 percent. *CNMI Comments*, at 4.

<sup>51</sup> See *First Report and Order*, 12 FCC Rcd at 8783, ¶ 8.

<sup>52</sup> *Id.*, 8843, ¶¶ 120-21.

<sup>53</sup> *Unserved and Underserved Areas Further Notice*, 14 FCC Rcd at 21233-37, ¶¶ 135-47.



“subscribership levels provide relevant information regarding whether consumers have the means to subscribe to universal service and, thus, represent an important tool in evaluating the affordability of rates.”<sup>54</sup>

Second, in the case of rural and high-cost areas, the Commission has previously interpreted section 254’s directive as requiring it to establish a funding mechanism to enhance universal service. In this provision, Congress identifies together rural, high-cost, and insular areas as in need of special attention. Based upon this directive, the Commission has set up specific universal service funding mechanism for high-cost and rural areas. From the plain language of the statute, there is no basis for according non-rural insular areas less assistance than these two other areas with unique concerns. Further, the facts of telecommunications service in non-rural insular areas – the extremely low penetration rates and very high costs of providing service – make clear that non-rural insular areas have not achieved Congress’ goal of affordable access. Accordingly, non-rural insular areas are just as deserving of assistance under the statute as rural and high-cost areas.

For these reasons, section 254 requires the Commission to address the unique universal service needs of all insular areas by establishing a non-rural insular mechanism. Given the passage of nine years since the enactment of section 254, prompt action by the Commission is required.

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<sup>54</sup> *First Report and Order*, 12 FCC Rcd at 8838-39, ¶ 112. The Joint Board further found a “general correlation between subscribership level and affordability.” *1996 Recommended Decision*, 12 FCC Rcd at 151-52, ¶ 127.

## **B. Public Interest Concerns Compel Commission Action**

In addition to the specific legal requirements of section 254, public interest considerations require the adoption of a funding mechanism to address the unique needs of non-rural insular areas. As discussed below, the conditions in non-rural insular areas necessitate the provision of high-cost universal service. Moreover, the FCC's adoption of the synthesis model for high-cost funding has exacerbated the situation in non-rural insular areas by eliminating all high-cost loop support previously received.

Although insular areas are not all the same, they share some characteristics that significantly increase the costs of providing telecommunications services, costs that generally do not vary based on the rural nature of the area served. In fact, the record demonstrates that the demographics and operational challenges faced by non-rural insular carriers are substantial and unique, similar to those experienced by rural insular carriers as well as rural mainland carriers.

### **1. Conditions in Insular Areas Necessitate Commission Action**

#### **a. Geographic Differences**

The most significant difference between insular and mainland areas is that insular areas are, by definition, separated from the rest of the United States by hundreds (and sometimes thousands) of miles of ocean. This requires that all the supplies necessary for creating and maintaining a telecommunications infrastructure be shipped and stored at considerable expense.<sup>55</sup> Some insular areas, like the inland areas of Puerto Rico, have rough, hilly terrain, or heavy vegetation, which results in "telecommunications transmission facilities requir[ing]

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<sup>55</sup> See *VIPSC Comments* at 3-4; Comments of the Government of Guam, CC Docket No. 96-45, at 5 (Dec. 17, 1999) ("*Guam Comments*"); *PRT Underserved Comments* at 6-7.

additional guying and anchoring and the distances between points [being] increased.”<sup>56</sup> These characteristics, when combined with the higher costs of securing supplies, often cause insular areas to lack basic infrastructure in some regions, such as passable and paved roads and, in some cases, electricity.<sup>57</sup>

The climate in insular areas is also a major factor in increasing the costs of providing telecommunications services. The salt air that pervades such areas is “corrosive and inhospitable to telecommunications equipment,” leading to accelerated deterioration.<sup>58</sup> Even more damaging is that many insular areas are located in common paths of severe tropical weather, requiring yearly reconstruction of existing infrastructure due to tropical storm and hurricane damage.<sup>59</sup> The combination of these geographic complications results in loop costs approximating, if not exceeding, those in rural communities.<sup>60</sup>

b. Economic Characteristics

The economic realities of living in both rural and non-rural insular areas further contributes to the low penetration rates and challenges faced by insular carriers. The incomes of the residents of U.S. insular areas are markedly lower than the incomes of most persons in

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<sup>56</sup> *VIPSC Comments* at 4; *see also PRT Underserved Comments* at 6-7.

<sup>57</sup> *See* Letter from Nancy J. Victory, Counsel for Puerto Rico Telephone Company, Inc., to Jeffrey Carlisle, CC Docket No. 96-45, 1-2 (filed Nov. 4, 2004) (“*November 2004 PRT Letter*”).

<sup>58</sup> *VIPSC Comments* at 4.

<sup>59</sup> *VIPSC Comments* at 4; *PRT Underserved Comments* at 7-8. Recently, Hurricane Jeanne caused \$11.5 million in damage to PRT’s facilities alone. *See* Letter from Nancy J. Victory, Counsel for Puerto Rico Telephone to Jeffrey Carlisle, CC Docket No. 96-45, at 2 (Mar. 28, 2005). (“*2005 PRT Letter*”).

<sup>60</sup> PRT has indicated that in some cases the cost for it to construct a single loop can be as much as \$15,000. *November 2004 PRT Letter* at 3.

mainland areas and comparable to those in tribal lands.<sup>61</sup> The per capita income of Puerto Rico is approximately two-thirds that of the poorest U.S. state.<sup>62</sup> Indeed, more than half of Puerto Rico's residents live below the poverty line.<sup>63</sup> Similarly, the per capita gross domestic product (GDP) of the U.S. Virgin Islands is approximately sixty percent of that of the mainland GDP.<sup>64</sup>

The challenges resulting from attempting to serve low-income populations are exacerbated by the high cost of living in many insular areas. For example, the cost of living index for Puerto Rico is 133.8, more than 30 points higher than the U.S. national average cost of living. This substantially higher index in Puerto Rico results from many of the same factors that increase the costs of providing telecommunications services there. In particular, the high cost of living is attributable to the need to ship materials and supplies to the island, the isolated nature of the island, as well as geographic and climatic-based costs.<sup>65</sup> Combining low per capita income with a dramatically higher cost of living translates to significantly less disposable income for residents of insular areas. Similarly, in the Virgin Islands, the average disposable income is 60 percent of that of the mainland.<sup>66</sup>

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<sup>61</sup> *Twelfth Report and Order*, 15 FCC Rcd at 12224-25, ¶ 27.

<sup>62</sup> *PRT Underserved Comments* at 8-9. (noting Puerto Rico's 1999 average income) Recent figures demonstrate that Puerto Rico lags substantially behind the mainland. Based on 2003 data, the per capita income of the United States is \$34,459. Puerto Rico is estimated to have a per capita income of \$16,800, or approximately two-thirds the income level of the poorest state, Mississippi (\$23,343), *2005 PRT Letter* at 2. Other insular areas also have below mainland-level incomes; the yearly per capita income of individuals in the Northern Mariana Islands is \$6,897. *CNMI Comments*, Exhibit at 3.

<sup>63</sup> *PRT Underserved Comments* at 8-9.

<sup>64</sup> *VIPSC Comments* at 5.

<sup>65</sup> *PRT Underserved Comments* at 10.

<sup>66</sup> *VIPSC Comments* at 5.

The lack of disposable income not only impacts the ability of low-income consumers to subscribe to telephone service, but also severely limits the ability of carriers to increase rates in order to fund infrastructure investment and improvement efforts.<sup>67</sup> The inordinate price sensitivity of low-income consumers also affects the ability of state commissions to initiate robust intrastate universal service funding efforts to ensure that all rural and underserved areas have modern infrastructures and facilities. For instance, the Telecommunications Regulatory Board of Puerto Rico (“TRB”) has been forced to limit its intrastate fund to low-income support programs because of the lack of intrastate resources to fund a larger support mechanism, or to offset high loop costs on the island.<sup>68</sup>

c. Demographic Differences

The demographic characteristics of insular areas also contribute to the challenges faced by both non-rural and rural insular communities. The population of insular areas is typically spread out across the territory of an island or island chain. Though many of these islands have one or two large population centers, they also have a significant number of citizens residing in remote, sparsely populated areas. The interior of Puerto Rico, the southern region of Guam, and certain portions of the Virgin Islands are all marked by low population densities over mountainous terrain.<sup>69</sup> In these areas, penetration rates tend to be much lower, while the costs of

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<sup>67</sup> As discussed in section II.B.3, the existence of low-income assistance alone cannot resolve the universal service problem because it does nothing to fund the investment necessary to expand telephone infrastructure and does not support higher maintenance costs found in insular areas.

<sup>68</sup> See *Ex Parte of Puerto Rico Telephone Company, Inc.*, CC Docket No. 96-45, 4 (Mar. 3, 2003).

<sup>69</sup> See *Guam Comments* at 3 (noting that “the southern region of Guam is a relatively sparsely populated, mountainous area where the cost of providing telephone service is high”); *PRT Underserved Comments* at 4-6 (illustrating that areas with low population densities also have low penetration rates); see also *VIPSC Comments* at 4 (indicating that “the bulk of the population

providing service are increased by the lack of economies of scale and scope as well as less hospitable terrain and higher equipment costs.<sup>70</sup> In sum, all insular providers face distinct hurdles to delivering a quality of service to all citizens commensurate with that on the mainland. As such, universal service support plays a pivotal role in insular areas, much as it does in rural America. Given the Commission's prudent and cautious course of action with respect to universal service policies for rural areas, including rural insular areas, the Commission should exercise at least as much caution with respect to non-rural insular areas.

## 2. Non-Rural Insular Areas Are Completely Overlooked by the FCC's Existing Funding Mechanisms

The FCC has created two distinct high-cost loop support mechanisms, neither of which provides sufficient funding to non-rural insular areas. First, the FCC adopted a rural high-cost loop mechanism that is limited to "rural telephone companies" as defined in the Act.<sup>71</sup> Non-rural insular carriers are not eligible to receive support under that program.

Second, the Commission created a general, or non-rural, high-cost loop mechanism based on a forward-looking cost model. The non-rural high cost mechanism has eliminated all high-cost loop support formerly received by non-rural insular carriers, in part because that mechanism's model is based on mainland assumptions and inputs. As a result, the high-cost model cannot adequately take into account the unique operational conditions in insular areas, or incorporate the lack of comparable economies of scale in insular communities. The disparate

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resides on the coastal regions of the territory, and, as a result, the bulk of the telecommunications facilities are found there as well").

<sup>70</sup> *PRT Underserved Comments* at 3-10.

<sup>71</sup> 47 U.S.C. § 153(37).

impact of the model on non-rural insular areas corroborates the concerns raised by insular commenters, and necessitates corrective action and further study to prevent additional harm to non-rural insular areas.

In the *Ninth and Tenth Reports and Order*, the Commission created the non-rural universal service mechanism based on costs derived from the synthesis model, a forward looking cost model.<sup>72</sup> The inputs to the synthesis model were obtained from national figures derived from mainland sources.<sup>73</sup> In applying the non-rural mechanism to non-rural insular areas, the FCC overlooked the Joint Board's recognition in its original Recommended Decision of the potential problem with applying a mainland model to insular areas: "while we believe that proxy models may provide an appropriate determination of costs on which to base high-cost support, we are less certain that they may do so for rural carriers in Alaska and insular areas."<sup>74</sup>

The FCC further failed to heed the warnings of state commissions that insular carriers may lack the requisite data to populate the model. Specifically, the TRB expressed concern that insular areas do "not have a systemic addressing system" and "[a customer's] address is not likely to have any relationship with the location of the addressee."<sup>75</sup> The lack of accurate and granular location data is particularly problematic because the FCC has found that that "the most significant portions of network costs will be determined using the model's customer location

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<sup>72</sup> See generally *Ninth Report and Order*; *Tenth Report and Order*.

<sup>73</sup> See e.g. *Tenth Report and Order*, 14 FCC Rcd at 20282, ¶ 299.

<sup>74</sup> *1996 Recommended Decision*, 12 FCC Rcd at 240, ¶ 298.

<sup>75</sup> Letter from Phoebe Forsythe Isales, Telecommunications Regulatory Board of Puerto Rico, to William E. Kennard, Chairman, FCC (filed Apr. 22, 1998).

module,”<sup>76</sup> and, in turn, that “the most accurate data for locating customers within wire centers are precise latitude and longitude coordinates for those customers’ locations.”<sup>77</sup> Mainland commenters also noted that “[s]erious questions are raised” by the fact that Puerto Rico’s carriers would not “qualify for support under the Commission’s new high-cost mechanism.”<sup>78</sup>

At its inception, the FCC’s decision to transition non-rural insular carriers to a forward-looking cost model in the *First Report and Order* was premised on the conclusion that such carriers should possess economies of scale and scope as much as non-rural carriers.<sup>79</sup> Yet the economies assumed in the *First Report and Order* do not in fact exist as a result of the idiosyncratic operational characteristics of insular areas. Puerto Rico is a case in point. Despite its relative size, PRT lacks the scope a similarly situated mainland carrier possesses because of disproportionately low penetration rates.<sup>80</sup> Moreover, because of geographic and climatic factors, Puerto Rico’s average loop cost is almost double that of carriers in non-insular areas, and bears little relation to the costs assumed with loops of similar length on the mainland.<sup>81</sup> Puerto Rico’s carriers also do not “serve[] a broad enough territory such that high-cost areas may be balanced against relatively low-cost, high density areas.”<sup>82</sup> The amalgamation of these factors

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<sup>76</sup> *Federal-State Joint Board on Universal Service; Forward Looking Mechanism for High Cost Support for Non-Rural LECs*, Fifth Report and Order, 13 FCC Rcd 21323, 21335-36, ¶ 27 (1998) (“*Fifth Report and Order*”).

<sup>77</sup> *Id.*, ¶ 33.

<sup>78</sup> Letter from Laurence G. Malone, Counsel for New York State Public Service Commission, to Hon. Magalie Roman Salas, Secretary, FCC, CC Docket No. 96-45, n.2 (filed Dec. 1, 1999).

<sup>79</sup> *First Report and Order*, 12 FCC Rcd at 8946, ¶ 315.

<sup>80</sup> PRT Petition for Reconsideration at 4.

<sup>81</sup> *Id.* at 11.



undermines the economies of scale and scope that a carrier like PRT would benefit from on the mainland, or that are assumed by the high-cost model.

The actual impact of the non-rural mechanism on insular areas largely confirms the warnings raised by insular carriers and state commissions serving insular areas. For example, PRT, the only non-rural insular carrier that had previously qualified for high-cost loop support using the previous universal service formula, received \$50 million in high-cost loop support in 2000 alone, the second highest amount in the country.<sup>83</sup> Yet in 2005, Puerto Rico will receive \$0.00 in high-cost loop support.<sup>84</sup> The non-rural mechanism has proven unable to reliably and accurately predict the costs and operational conditions of serving Puerto Rico, as PRT's embedded costs are two and half standard deviations higher than the synthesis model produces.<sup>85</sup> PRT has additionally reported that the model underestimates the total line count in Puerto Rico by 18 percent – projecting only 1.09 million lines even though PRT operates over 1.29 million lines – the largest disparity of any carrier under the non-rural fund.<sup>86</sup>

The impact of eliminating all funding to Puerto Rico has been significant and not without direct effect on conditions in Puerto Rico. After decades of an incremental rise in capital expenditures and subscribership rates, PRT demonstrated that its capital investment budget and

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<sup>82</sup> *Id.* at 12.

<sup>83</sup> *Universal Service Monitoring Report*, Federal Communications Commission, Wireline Competition Bureau, CC Docket No. 98-202, 3-19 (Table 3.8) (rel. Dec. 22, 2003) (“*2003 Monitoring Report*”).

<sup>84</sup> *November 2004 PRT Letter* at 2.

<sup>85</sup> *See 2005 PRT Letter* at 4.

<sup>86</sup> *Id.*

the island's subscribership levels have stagnated, if not receded, since the synthesis model was applied to Puerto Rico and funding was eliminated.<sup>87</sup>

These types of cost comparisons, and the full impact of the non-rural mechanism on insular areas, were unavailable at the time the Commission made its original determination to adopt the model. Given the factual record that is now before the Commission, the FCC can no longer support the continued treatment of insular areas, especially Puerto Rico, under the mainland non-rural mechanism.<sup>88</sup>

### 3. High-Cost Loop Support Complements Other Universal Service Support Mechanisms

The Commission's universal service program is comprised of a set of complementary programs that work in conjunction to ensure that consumers have access to affordable and reasonably comparable telecommunications services. The Commission's loop support programs (non-rural and rural high-cost mechanisms) provide carriers with funding to offset the intrastate cost to provide loop access to end-users. The Commission's low-income programs (Lifeline and Link-Up) provide discounted services directly to eligible end-user customers.<sup>89</sup> Finally, the Commission's access support programs (Interstate Common Line Support and Interstate Access Support), in turn, are directed to carriers in order to reduce the long distance and interstate access

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<sup>87</sup> See November 2004 PRT Letter at 7.

<sup>88</sup> These circumstances justify the Commission adopting a modification to the original Joint Board Recommendation that would have continued to use embedded costs for only rural insular carriers as outlined herein.

<sup>89</sup> The Commission has noted that the Lifeline and Link-Up programs were created to "provide assistance for low-income consumers to get connected and stay connected to the telecommunications network." *Federal-State Joint Board on Universal Service, Access Charge Reform*, Seventh Report & Order and Thirteenth Order on Reconsideration in CC Docket No. 96-45, Fourth Report and Order, 14 FCC Rcd 8078, 8096-97, ¶ 39 (1999) ("*Seventh Report and Order*").

costs of serving a community. Each of these programs targets a different need. Thus, in high-cost and poor communities, high-cost loop and access support traditionally has been available, in addition to low-income support, to address infrastructure and system-wide maintenance and quality of service issues that need to be rectified so that all Americans can have a basic level of telecommunications service.

Because low-income support is a straight pass-through to consumers, it functions only to increase subscribership where consumers already have access to the telecommunications infrastructure. Thus, this mechanism alone cannot provide adequate assistance to a carrier to build new infrastructure to serve previously unserved areas (where such costs exceed the average costs to provide service to all consumers in a study area), nor does it provide sufficient funding to upgrade and maintain existing network facilities. This is particularly true in an area, such as Puerto Rico, that has over 200 communities that do not have access to telecommunications service.<sup>90</sup>

As the Commission noted in the *Seventh Report and Order*, “section 254(b)(3) reflects a legislative judgment that all Americans, regardless of income, should have access to the network at reasonably comparable rates.”<sup>91</sup> This can only be achieved if the basic network infrastructure is extended to all Americans. Thus, despite the fact that the Commission has continued to expand the Lifeline and Link-Up programs<sup>92</sup> by increasing the amount of money available under

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<sup>90</sup> *November 2004 PRT Letter* at 2.

<sup>91</sup> *Seventh Report and Order*, 14 FCC Rcd at 8096-97, ¶ 39.

<sup>92</sup> The Lifeline support program is designed to increase subscribership by reducing qualifying low-income consumers’ monthly basic local charge. *See* 47 C.F.R. § 54.401 (2004). The Link-Up program assists qualifying low-income consumers in initiating telephone service by paying a

those programs<sup>93</sup> and broadening the eligibility criteria,<sup>94</sup> low penetration continues to be a problem in non-rural insular areas.

Similarly, a carrier's receipt of interstate access support does not address the need to offset high intrastate loop costs in a jurisdiction. For instance, Puerto Rico currently receives interstate common line support ("ICLS") funding to offset significantly high interstate access costs, separate and distinct from the high intrastate loop costs for which non-rural insular support would be directed.<sup>95</sup>

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portion of the service connection charge. *See* 47 C.F.R. § 54.411 (2004). The Commission adopted Lifeline/Link-Up prior to passage of the Act pursuant to its general authority under sections 1, 4(i), 201, and 205 of the Act. *See First Report and Order*, 12 FCC Rcd at 8952-53, ¶ 329; 47 U.S.C. §§ 151, 154(i), 201, 205.

<sup>93</sup> The Commission increased Lifeline support to offset an increase in the Subscriber Line Charge. *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Second Report and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd 19613, 19689, ¶ 178 (2001) ("MAG Order").

<sup>94</sup> In April 2004, the Commission expanded the eligibility criteria for Lifeline and Link-Up to include any consumer whose income is 135 percent or less of the Federal Poverty Guidelines. Previously, consumers were only eligible if they took part in Medicaid, Food Stamps, Supplemental Security Income (SSI), Federal Public Housing Assistance (section 8) (FPHA), or the Low Income Home Energy Assistance Program (LIHEAP). The Commission also encouraged states to implement automatic enrollment in Lifeline and Link-Up, though it stopped short of requiring automatic enrollment. *Lifeline and Link-Up*, Report and Order and Further Notice of Proposed Rulemaking, 19 FCC Rcd 8302, 8307-12, 8318-19, ¶¶ 7-13, 25-26.

<sup>95</sup> *See MAG Order*, 16 FCC Rcd at 19667-8, ¶ 128; *see also* 47 C.F.R. §§54.901-904. The Commission established the IAS mechanism as part of a five-year transitional access charge and universal service reform plan for price cap carriers. *Access Charge Reform, Price Cap Performance Review for LECs*, Sixth Report and Order, 15 FCC Rcd 12962, 13049-55, ¶¶ 206-13 (2000) (subsequent history omitted). No insular carrier currently receives IAS, PRT operates under a waiver of the all-or-nothing rule. *See ALLTEL Corporation Petition for Waiver of section 61.41, ALLTEL Corporation Petition to Extend Interim Waiver of section 61.41 of the Commission's Rules, CenturyTel, Inc. and CenturyTel of Alabama, LLC Petition for Waiver of sections 61.41(b) and (c) of the Commission's Rules, CenturyTel, Inc. and CenturyTel of Missouri, LLC Petition for Waiver of sections 61.41(b) and (c) of the Commission's Rules, Puerto Rico Telephone Company Petition for Waiver of section 61.41 of the Commission's Rules or, in the Alternative, Request for Waiver of section 54.303(a) of the Commission's Rules*,

Because these different universal service programs target different issues, the unavailability of high-cost support for non-rural insular areas is a substantial disadvantage. Mainland carriers, or their customers, serving both rural and non-rural areas receive support, often substantial support, from all three major categories of support mechanisms: high-cost loop support, access support and low-income support, while Puerto Rico receives only access and low-income support under the FCC's current rules.<sup>96</sup> The continued lack of sufficient funding to Puerto Rico from each universal service program cannot be supported by this record, and is inconsistent with the treatment of similarly situated areas.

### **III. NON-RURAL INSULAR HIGH-COST LOOP SUPPORT MECHANISM**

As detailed above, at a minimum, section 254 and the public interest require that the Commission adopt an interim rule for non-rural insular carriers<sup>97</sup> to ensure that the citizens of all insular areas obtain access to affordable telecommunications services. Given that a number of insular carriers currently receive support based on embedded costs because they are classified as “rural,” there is no need to establish an insular mechanism applicable to rural insular carriers. Consistent with the limited nature of this mechanism, the non-rural insular fund would have a negligible impact on the total universal service fund.

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Memorandum Opinion and Order, 17 FCC Rcd 27694 (2002); *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*; *Federal-State Joint Board on Universal Service*, Report and Order and Second Further Notice of Proposed Rulemaking, 19 FCC Rcd 4122 (2004).

<sup>96</sup> *Universal Service Monitoring Report*, CC Docket No. 98-202, (Tables 2.5, 3.24, 3.27) (Oct. 12, 2004) (“2004 Monitoring Report”).

<sup>97</sup> Insular carriers have been defined herein as those providers serving islands that are territories or commonwealths of the United States.

1. The Commission should adopt an interim solution for non-rural insular areas.

Until the Commission has in place a forward-looking cost mechanism that can accurately identify costs for all non-rural insular areas, the Commission should adopt a new interim mechanism for non-rural insular areas that is patterned after, but distinct from, the existing mechanism in place for rural telephone companies.<sup>98</sup> Toward this end, a proposed new rule establishing such a mechanism is attached as Appendix A.<sup>99</sup> Under this approach, federal high-cost funding would be available for those non-rural insular study areas in which the average unseparated cost per loop exceeds 115 percent of the national average loop cost.

Adoption of new interim rules for non-rural insular carriers will provide necessary resources to ensure continued infrastructure investment and expansion in insular areas.<sup>100</sup> The provision of explicit and sufficient universal service high-cost loop support to all insular carriers – either pursuant to the rural mechanism or the proposed non-rural insular mechanism – satisfies

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<sup>98</sup> Procedurally, the Commission has a number of active proceedings under which the non-rural mechanism could be adopted. In the *Unserved and Underserved* docket, the *Twelfth Report and Order* addressed only the tribal lands portion of the proceeding, and the Commission explicitly "defer[ed] consideration of any issues raised in the *Further Notice* that are not addressed in this Order." *Twelfth Report and Order*, ¶ 12. The FCC also pledged to "continue to examine and address the causes of low subscribership in other areas," referencing insular areas. *Id.*, ¶ 11. No subsequent action has been taken with respect to insular areas, and action in that proceeding is overdue. The Commission could also act on PRT's January 2004 petition for clarification and/or reconsideration of the FCC's *Ninth Report Remand Order*, which denied a prior PRT request for insular funding. See *PRT Petition for Clarification*.

<sup>99</sup> Although the Commission could create a completely distinct new type of mechanism for non-rural insular carriers or expend significant resources to adjusting the synthesis model to address insular issues, neither of these options is feasible at this time. First, either option would take substantial time and resources, which would risk further potential harm to insular carriers. Second, relying on a mechanism that has been used on an interim basis for rural carriers has the advantage that it produces known results that the Commission can assess and predict.

<sup>100</sup> This new rule as a practical matter would impact only the Commonwealth of Puerto Rico since it is the only high-cost insular area that is not currently classified as a rural carrier under the rural high-cost loop mechanism.

the mandate of section 254, and promotes the delivery of mainland-level availability and quality of telecommunications service to U.S. territories.

2. The non-rural insular mechanism would have limited impact on the universal service fund

The adoption of this mechanism is consistent with the continued sustainability of the universal service fund and the need to protect “against excessive fund growth.”<sup>101</sup> The non-rural insular mechanism would restore funding only to non-rural insular areas, approximately \$40 million in annual funding using 2001 data.<sup>102</sup> This would be consistent with, but lower than, the support levels prior to the adoption of the non-rural mechanism.

Accordingly, this mechanism does not provide new or expanded support to any area, it is only a correction in FCC policy, returning funding that should never have been phased out. Further, the new mechanism would provide support to only one jurisdiction, Puerto Rico, further limiting any risk that such a fund could grow excessively in the future. The total cost of the new fund would be less than 1 percent of the total fund, underscoring the targeted and limited nature of these reforms.<sup>103</sup>

#### IV. CONCLUSION

For the foregoing reasons, Commission must take prompt action to adopt a high-cost loop support mechanism for non-rural insular areas.

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<sup>101</sup> *Referral Order*, 19 FCC Rcd at 11538, ¶ 1.

<sup>102</sup> *PRT Petition for Clarification* at 22.

<sup>103</sup> In 2003, the cost of all the universal service support mechanisms was over \$5 billion. *2004 Monitoring Report*, at 1-36 (Table 1.11).

**Subpart L – Non-Rural Insular High-Cost Loop Support Mechanism**

**§ 54.1001. Eligibility.**

(a) Non-rural insular high-cost loop support is available to eligible telecommunications carriers that serve islands that are territories or commonwealths of the United States, and are not classified as a “rural telephone company,” as defined in § 51.5 of this chapter.

**§ 54.1002. Calculation of Non-Rural Insular High-Cost Loop Support.**

(a) For non-rural insular study areas reporting 200,000 or fewer working loops pursuant to § 36.611(h) the expense adjustment (additional interstate expense allocation) is equal to the sum of paragraphs (a)(1) through (2) of this section.

(1) Sixty-five percent of the study area average unseparated loop cost per working loop as calculated pursuant to § 36.622(b) in excess of 115 percent of the national average for this cost but not greater than 150 percent of the national average for this cost as calculated pursuant to § 36.622(a) multiplied by the number of working loops reported in § 36.611(h) for the study area; and

(2) Seventy-five percent of the study area average unseparated loop cost per working loop as calculated pursuant to § 36.622(b) in excess of 150 percent of the national average for this cost as calculated pursuant to § 36.622(a) multiplied by the number of working loops reported in § 36.611(h) for the study area.

(b) For non-rural insular study areas reporting more than 200,000 working loops pursuant to § 36.611(h), the expense adjustment (additional interstate expense allocation) is equal to the sum of paragraphs (b)(1) through (4) of this section.

(1) Ten percent of the study area average unseparated loop cost per working loop cost per working loop as calculated pursuant to § 36.622(b) in excess of 115 percent of the national average for this cost but not greater than 160 percent of the national average for this cost as calculated pursuant to § 36.622(a) multiplied by the number of working loops reported in § 36.611(h) for the study area;

(2) Thirty percent of the study area average unseparated loop cost per working loop as calculated pursuant to § 36.622(b) in excess of 160 percent of the national average for this cost but not greater than 200 percent of the national average for this cost as calculated pursuant to § 36.622(a) multiplied by the number of working loops reported in § 36.611(h) for the study area;

(3) Sixty percent of the study area average unseparated loop cost per working loop as calculated pursuant to § 36.622(b) in excess of 200 percent of the national average for



this cost but not greater than 250 percent of the national average for this cost as calculated pursuant to § 36.622(a) multiplied by the number of working loops reported in § 36.611(h) for the study area; and

(4) Seventy-five percent of the study area average unseparated loop cost per working loop as calculated pursuant to § 36.622(b) in excess of 250 percent of the national average for this cost as calculated pursuant to § 36.622(a) multiplied by the number of working loops reported in § 36.611(h) for the study area.

#### **54.1003. Disaggregation and targeting of high-cost support.**

(a) All non-rural insular carriers on or before May 15, 2005 must select a disaggregation path as described in paragraphs (b), (c), or (d) of this section. In study areas in which a competitive carrier was designated as a competitive eligible telecommunications carrier prior to June 19, 2001, the non-rural insular carrier may only disaggregate support pursuant to paragraphs (b), (c), or (d)(1)(iii) of this section. A non-rural insular carrier failing to select a disaggregation path as described in paragraphs (b), (c), or (d) of this section by May 15, 2005, will not be permitted to disaggregate and target federal high-cost support unless ordered to do so by a state commission as that term is defined in § 54.5.

##### **(b) Path 1: Carriers Not Disaggregating and Targeting High-Cost Support:**

(1) A carrier may certify to the state commission that it will not disaggregate and target high-cost universal service support.

(2) A carrier's election of this path becomes effective upon certification by the carrier to the state commission.

(3) This path shall remain in place for such carrier for at least four years from the date of certification to the state commission except as provided in paragraph (b)(4) of this section.

(4) A state commission may require, on its own motion, upon petition by an interested party, or upon petition by a non-rural insular carrier, the disaggregation and targeting of support under paragraphs (c) or (d) of this section.

(5) A carrier not subject to the jurisdiction of a state, *e.g.*, certain tribally owned carriers, may select Path 1, but must certify to the Federal Communications Commission as described in paragraphs (b)(1) through (4) of this section.

##### **(c) Path 2: Carriers Seeking Prior Regulatory Approval for the Disaggregation and Targeting of Support:**

(1) A carrier electing to disaggregate and target support under this paragraph must file a disaggregation and targeting plan with the state commission.

(2) Under this paragraph a carrier may propose any method of disaggregation and targeting of support consistent with the general requirements detailed in paragraph (e) of this section.

(3) A disaggregation and targeting plan under this paragraph becomes effective upon approval by the state commission.

(4) A carrier shall disaggregate and target support under this path for at least four years from the date of approval by the state commission except as provided in paragraph (c)(5) of this section.

(5) A state commission may require, on its own motion, upon petition by an interested party, or upon petition by a non-rural insular carrier, the disaggregation and targeting of support in a different manner.

(6) A carrier not subject to the jurisdiction of a state, *e.g.*, certain tribally owned carriers, may select Path 2, but must seek approval from the Federal Communications Commission as described in paragraphs (c)(1) through (5) of this section.

(d) Path 3: Self-Certification of the Disaggregation and Targeting of Support:

(1) A carrier may file a disaggregation and targeting plan with the state commission along with a statement certifying one of the following:

(i) It has disaggregated support to the wire center level; or

(ii) It has disaggregated support into no more than two cost zones per wire center; or

(iii) That the carrier's disaggregation plan complies with a prior regulatory determination made by the state commission.

(2) Any disaggregation plan submitted pursuant to this paragraph must meet the following requirements:

(i) The plan must be supported by a description of the rationale used, including the methods and data relied upon to develop the disaggregation zones, and a discussion of how the plan complies with the requirements of this paragraph. Such filing must provide information sufficient for interested parties to make a meaningful analysis of how the carrier derived its disaggregation plan.

(ii) The plan must be reasonably related to the cost of providing service for each disaggregation zone within each disaggregated category of support.

(iii) The plan must clearly specify the per-line level of support for each category of high-cost universal service support provided pursuant to § 54.1002 of this chapter in each disaggregation zone.

(iv) If the plan uses a benchmark, the carrier must provide detailed information explaining what the benchmark is and how it was determined. The benchmark must be generally consistent with how the total study area level of support for each category of costs is derived to enable a competitive eligible telecommunications carrier to compare the disaggregated costs used to determine support for each cost zone.

(3) A carrier's election of this path becomes effective upon certification by the carrier to the state commission.

(4) A carrier shall disaggregate and target support under this path for at least four years from the date of certification to the state commission except as provided in paragraph (d)(5) of this section.

(5) A state commission may require, on its own motion, upon petition by an interested party, or upon petition by a non-rural insular carrier, modification to the disaggregation and targeting of support selected under this path.

(6) A carrier not subject to the jurisdiction of a state, e.g., certain tribally owned carriers, may select Path 3, but must certify to the Federal Communications Commission as described in paragraphs (d)(1) through (5) of this section.

(e) Additional Procedures Governing the Operation of Path 2 and Path 3: Disaggregation and targeting plan adopted under paragraphs (c) or (d) of this section shall be subject to the following general requirements:

(1) Support available to the carrier's study area under its disaggregation plan shall equal the total support available to the study area without disaggregation.

(2) The ratio of per-line support between disaggregation zones for each disaggregated category of support shall remain fixed over time, except as changes are allowed pursuant to paragraph (c) and (d) of this section.

(3) The ratio of per-line support shall be publicly available.

(4) Per-line support amounts for each disaggregation zone shall be recalculated whenever the carrier's total annual support amount changes using the changed support amount and lines at that point in time.

(5) Per-line support for each category of support in each disaggregation zone shall be determined such that the ratio of support between disaggregation zones is maintained and that the product of all of the carrier's lines for each disaggregation zone multiplied by the

per-line support for those zones when added together equals the sum of the carrier's total support.

(6) Until a competitive eligible telecommunications carrier is certified in a study area, monthly payments to the incumbent carrier will be made based on total annual amounts for its study area divided by 12.

(7) When a competitive eligible telecommunications carrier is certified in a study area, per-line amounts used to determine the competitive eligible telecommunications carrier's disaggregated support shall be based on the incumbent carrier's then-current total support levels, lines, and disaggregated support relationships.

(f) Submission of Information to the Administrator:

(1) A carrier certifying under paragraph (b) of this section that it will not disaggregate and target high-cost universal service support shall submit to the Administrator a copy of the certification submitted to the state commission, or the Federal Communications Commission, when not subject to state jurisdiction.

(2) A carrier electing to disaggregate and target support under paragraph (c) of this section shall submit to the Administrator a copy of the order approving the disaggregation and targeting plan submitted by the carrier to the state commission, or the Federal Communications Commission, when not subject to state jurisdiction, and a copy of the disaggregation and targeting plan approved by the state commission or the Federal Communications Commission.

(3) A carrier electing to disaggregate and target support under paragraph (d) of this section shall submit to the Administrator a copy of the self-certification plan including the information submitted to the state commission pursuant to paragraphs (d)(2)(i) and (d)(2)(iv) of this section or the Federal Communications Commission.

(4) A carrier electing to disaggregate and target support under paragraph (c) or (d) of this section must submit to the Administrator maps which precisely identify the boundaries of the designated disaggregation zones of support within the carrier's study area.